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SENATOR BILL MORROW



CAPITOL UPDATE

Major Issues Pending for End of Session

This report provides a brief overview of the major issues before the Legislature during the final weeks of session. This year began with the Energy Crisis, and this issue will continue to dominate as attempts are made to resolve the Southern California Edison MOU. The once-a-decade redistricting plan will also be decided. In addition, issues ranging from bonds to fully endangered species will be hot topics. Between now and September 14, up to 700 bills will hit the Senate Floor for votes. As always, I welcome your input regarding any and all issues that are of concern to you.

-- Bill Morrow

Redistricting

New district lines for Congressional, Senate, Assembly and Board of Equalization districts must be approved by the Legislature before the end of session. The Assembly unveiled their plans August 29. Assembly rules call for a 7-day public comment period before the maps can be voted upon. The Senate does not have a rule regarding the public comment period.

This year's reapportionment is unique in California history. Term limits, new technology and the early primary make it difficult for the Democrats to reach an agreement without Republican support. Several ethnic communities are actively participating in the redistricting process. Los Angeles County is losing roughly $\frac{3}{4}$ of Senate Seat, $1\frac{1}{2}$ of an Assembly and a Congressional seat. Each of these issues will increase the difficulty of creating plans for new districts.

Since 1970, the first reapportionment bill has always failed to be implemented. The last redistricting conducted with a Democratically-controlled Governor and Legislature in the eighties resulted in a referendum sponsored by Republicans.

Senate Republicans support a plan that follows good government principles and keeps communities of interest together. The plan should also reflect the state's ethnic and political diversity.

Energy

◆ Edison MOU

The MOU discussion is still intertwined with the discussions on the \$12.5 billion energy bond and CPUC decisions that are required for the issuance. Governor Davis recently announced the outlines of a new MOU. In addition, there are three bills dealing with the MOU. It is unclear which version, if any, will survive. The key distinctions between the bills and the original and revised Governor's proposals include:

<u>Provision</u>	<u>Orig. MOU</u>	<u>New MOU</u>	<u>SB 78xx Polanco/ Sher</u>	<u>AB 82xx Keeley</u>	<u>AB 83xx Wright</u>
Transmission line price	\$2.76B	\$1.2B	\$1.2B	\$2.4B	n/a
Multiple of book value	2.3	1.0	1.0	2.0	n/a
Transmission deal	purchase	option	option	purchase	n/a
Debt Assistance	\$3.5B	\$2.9B	\$2.5B	\$3.5B	\$3.5B
Bonds paid by	customers	business	business	all - 1 st 2 yrs; then business	all
Conservation lands	yes	yes		yes	no
Cheap power for state	yes	yes	yes	yes	??
Parent contribution	\$400M	\$400M	\$400M	\$500M	none
Direct Access	no	limited	not addressed	yes	yes

In addition to the Edison MOU, the Legislature is expected to vote on legislation regarding the San Diego Gas & Electric MOU. However, no bill has yet to be introduced.

◆ DWR Power Purchases

Senate and Assembly Republicans have called for legislative hearings regarding all long-term energy contracts entered into and spot-market purchases made by the Davis Administration. Recent press accounts have disclosed disturbing trends of power contracts that are priced too high; significant conflict of interest problems for the power traders hired by DWR; and sales of contracted power at exorbitant losses. Although there is no current legislation, meaningful oversight, such as a reasonableness review, is desirable but would put the bond issuance at risk.

◆ **Power Plant Facilities and Property Tax Allocations**

Because power plants generate little or no sales tax revenue and because counties and cities keep only a small portion of property tax revenue, local officials have little fiscal incentive to site power plants. By allowing a city or county to keep some of the new property tax revenues generated from a power plant, a strong fiscal incentive to cities and counties is created to site new power plants, giving them an important tool to combat local opposition.

Power Plant Facilities Legislation

- ◆ ***SB 30XX (Brulte)***—Allocates property tax revenues from new electrical generation facilities or new modifications to existing facilities entirely to the city or county in which the primary power-generation operation is located. The property tax revenues generated are exempted from ERAF.
- ◆ ***AB 31 XX (Cohn)***—Provides a financial incentive to local governments to approve siting of power generating facilities within their jurisdiction.
- ◆ ***SB 1019 (Torlakson)***—Shifts property tax revenues from power-plant facilities that have multi-county operations that act as a unit from being allocated among all the counties in which the property is located. Instead these property tax revenues would be allocated solely to the county in which the primary electrical generating facility is located.
- ◆ ***AB 226 (Bill Campbell)***—Changes the allocation of property tax revenues derived from new and repowered power plant facilities and requires the Public Utilities Commission to issue certain findings during the process of certifying new power generating facilities.

Education

◆ **Community College Funding**

In December, Republicans made providing community colleges with 11% of the Proposition 98 split a top budget priority. The Governor's January Budget proposed 10.27% of Proposition 98 funds for community colleges. But, the final budget gave community colleges a mere 10.2% – the lowest level in seven years – for a General Fund growth over 2000-01 of only 3.2 percent. In fact, 23% of all the funds vetoed by the Governor – \$126 million – came from the community college budget.

With the stroke of a blue pencil, the Governor eliminated \$49 million in base funding for schedule maintenance projects, ending a twenty-year commitment to community colleges and losing the leverage of a local match in the process. This will delay or eliminate scheduled

projects like roof replacements, the addition of security lighting, and the replacement of fire alarms – even a fire alarm for a child care center. The Governor also eliminated funding for instructional equipment, library materials replacement, Cal-Grant implantation, a COLA for the Partnership for Excellence, and for nurse training.

Several bills have been introduced to restore these funds to California community colleges. Both Republicans and Democrats have criticized the Governor's vetoes and a significant community college bill is likely before the end of next session.

◆ School Facilities Conference Committee

About one in three California school children attends an overcrowded school or a school in need of modernization. The State Allocation Boards puts a \$30 billion price tag on correcting these problems statewide. Roughly every two or three years, the legislature places a general obligation bond measure on the ballot to finance part of the cost of constructing and remodeling schools. In 1998, voters approved Proposition 1A to assist with \$9.2 billion in state matching funds for school facilities.

In the past, the State Allocation Board has awarded state bond funds on a first-come, first-serve basis. That allowed local school districts with available land and efficient facilities departments to build more schools. But a Los Angeles Superior court judge ruled in *Godinez v. Davis* that the wording of Proposition 1A required the State Allocation Board to enact a "priority points" system that considers need over speed. The State Allocation Board did so, setting aside for Los Angeles \$450 million of the school bond facilities and leaving many other school districts out in the cold, even though they played "by the rules."

The facilities bond and remaining facilities bills will go to conference committee. The key issues the conference committee must address are:

- The amount of the bond (could be as high as \$18 billion);
- Changes required by the *Godinez* lawsuit;
- On which ballot – primary or general – to place the bond measure;
- What set-asides should be made and for whom;
- Whether there should be a separate bond or an allotment for higher education.

If there is a facilities bond, Republicans should seek assurances that established bond priorities cannot be changed with subsequent legislation. Republicans should push for the repeal of the Field Act because it drives up the cost of facilities and is unnecessarily proscriptive, particularly for community colleges. Republicans should support reform of the State Allocation Board. Finally, Republicans should continue to push for pay-as-you-go funding for schools.

School Facilities Legislation

- ***AB 12 (Firebaugh)***—School facilities spot bill that contains intent language to address the school facilities issue in a more consistent way than issuing a general obligation bond. Uses the language from the LAO facilities report.
- ***AB 14 (Goldberg)***—Spot bill that expresses legislative intent to address facilities needs. The author has made it clear that this bill is intended to help LAUSD.
- ***AB 16 (Hertzberg)***—Kindergarten-University Public Education Facilities Bond Act of 2002. This is the designated vehicle for the facilities bond.
- ***AB 1072 (Cedillo)***—Allows state facilities bond money to be used to pay lease payments to private developers. Ignores legislation last year that prohibited such action.
- ***AB 1430 (Cardenas)***—Changes the existing formula for site acquisition for school construction to allow districts to receive funding based on appraised value within six months of the date of application rather than at the time of submission. Benefits LAUSD.
- ***AB 1580 (Cardenas)***—Reserves school facilities money for favored districts before they are ready to build schools. Will deprive other districts that have followed the established procedures of facilities funding and give it to districts whose administration is not competent enough to figure out how to construct schools.

♦ Low Performing Schools Conference Committee

Many of the bills on low-performing schools are also going to conference committee. To put it simply, most of these bills throw a lot of money to these schools with no accountability. They will allow schools that did not apply for the existing Immediate Intervention/Underperforming Schools Program (IIUSP) to circumvent the accountability requirements in the IIUSP.

Real reform for low performing schools would require those schools in the lowest two deciles to participate in a systemic schoolwide improvement program with a real accountability component. The sanctions timeframe must be parallel to the IIUSP. Merit/differential pay or stipends should be option.

Low Performing Schools Legislation

- ***SB 466 (Ortiz)***—Provides up to \$400 per pupil for schools in the lowest two deciles on the condition that they accomplish certain tasks such as have clean facilities, provide parental involvement, use research-based strategies, use multiple assessments, and other common sense teaching practices.
- ***SB 508 (Vasconcellos)***—Makes numerous changes to school facilities, teachers retirement, recruitment programs, parent involvement programs and more for the purpose of improving low-performing schools. This is a comprehensive act intended to provide many different ways of improving education but lacks an effective accountability component.
- ***AB 481 (Diaz)***—Allocates an unspecified amount of funding to schools in the lowest 2 deciles on the API. As a condition of receiving the money, schools must submit a plan for how the money will be used to attract and retain qualified teachers and involve parents. Provides no accountability or sanctions.
- ***AB 961 (Steinberg)***—Establishes another teacher recruitment and retention program for low-performing schools that are not in the IIUSP. Provides funding on the condition that the schools meet specified criteria such as clean facilities, standards aligned textbooks, and measurable progress on the API.
- ***AB 312 (Wesson)***—Creates the Middle Grades Reading Competency Act of 2001. Places legislative emphasis where it belongs: on the basics of reading and writing. Remedies the effects on these students of the failed philosophy of whole language, which completely failed to teach them to read.
- ***AB 226 (Goldberg)***—Creates a pilot project to demonstrate the value of school librarians.

◆ **The Standardized Testing and Reporting Program (STAR Test)**

SB 233 (Alpert) will reauthorize the STAR test. The current test is the same year after year. The Stanford 9 portion of the test is not aligned to current state standards. These as well as a myriad of other issues related to the reliability and validity of the test need to be addressed in the reauthorization.

◆ **Charter Schools**

Charter schools have been under assault this year. ***SB 740 (O'Connell)*** and ***AB 1132 (Canciamilla)*** both treat charter schools differently than regular schools and take away funding and flexibility, especially in the area of supplemental instruction. Supplemental instruction is usually offered as remedial instruction for students who are not achieving academically. It can be

offered before school, after school, during vacations, weekends, or inter-session. Schools that offer supplemental instruction get additional funding. SB 740 requires charter schools to get approval from the State Board to offer “non-classroom-based instruction,” and AB 1132 prohibits charters from offering supplemental instruction except on Saturday.

Transportation

◆ Bay Bridge Retrofit

A large issue looming in the Transportation area is how to pay for cost overruns of the Bay Bridge seismic retrofit. This issue has been further complicated by a dispute between Caltrans and the Metropolitan Transportation Commission (MTC) over the amount of the overrun. Caltrans initially estimated a cost of \$1.3 billion to retrofit the Bay Bridge. In April, however, they raised that estimate to \$2 billion and now claim that the project cost will increase \$3.5 million per week until work on the project commences.

In 1997, the Legislature enacted SB 60 (Kopp) Chapter 327, and SB 226 (Kopp), Chapter 328. These measures, among other things, established a \$1 surcharge on the tolls collected on the seven Bay Area state-operated toll bridges – Antioch, Benicia, Carquinez, Dumbarton, Richmond-San Rafael, San Mateo-Hayward, and the Bay Bridge. (The Golden Gate Bridge is not included and its retrofit was handled separately.)

The toll surcharges were expected to fund one-third of the estimated \$2.6 billion price tag for seismic retrofit. Under SB 60, one-third of the program costs would come from the State Highway Account (SHA), and the other third would come from Proposition 192, the Seismic Retrofit Bond Act of 1996.

SB 60 also required Caltrans to report to the Legislature within 60 days of determining that the actual cost of bridge retrofit or replacement exceeds \$2.6 billion. In April, Caltrans detailed the cost overruns and provided a funding scenario for addressing the cost overrun on four of the five state-owned toll bridges. Caltrans noted the limited options for funding any cost increase. The most likely option is extending the current \$1 toll surcharge.

The funds authorized under SB 60 are separate from those provided under Regional Measure 1, a uniform \$1 base toll for autos approved by Bay Area voters in 1988. Collection of toll surcharges authorized under SB 60 started on January 1, 1998. SB 60 established the surcharge for eight years, with an option for two additional years, if MTC chose a cable suspension span for the replacement eastern Bay Bridge. MTC recommended this type of span in July 1997. The current toll surcharges are scheduled to cease by January 1, 2008.

This year the Legislature must decide how the cost of the bridge work should be split between state and local funding. While Caltrans favors the state paying for one-third of the total cost, with local government paying for the remaining two-thirds, Bay Area Democrats will likely push for a greater percentage of funding to come from the state.

Health

◆ Provider Group and HMO Contractual Disagreements

In the past year there have been several contract disputes between HMO's and large provider groups that were not resolved prior to contract termination. The result was confusion as thousands of enrollees faced disruption of care. Normally issues between the plans and the provider groups are resolved just prior to cancellation and the enrollees are not effected.

Two bills were introduced this session to minimize disruptions in care following contract termination by requiring contracts between providers and plans. The outstanding difference between the two bills is how much above the prior rate should the provider groups be paid after the contract expires.

Providers fear that requiring them to continue to provide care for enrollees for up to 6 months after the contract expired is unfair if they are not given an adequate rate increase. Plans worry that requiring them to pay a statutorily created rate to providers in excess of a "reasonable" amount is also unfair. Much of the health care legislation this year is a variation of the larger problem of insolvency of provider groups and the fairness of the "capitated rate" system.

◆ Expansion of Healthy Families and Medi-Cal

The Legislature will decide whether to expand Healthy Families and Medi-Cal in the final weeks of the session. AB 32 (Richman) provides expanded health coverage to all persons under 250% Federal Poverty Level (FPL) through the Medi-Cal and Healthy Families programs. The two programs would be renamed as the Cal Health insurance program. The author believes that it is better public policy to provide this coverage in a manner that maximizes the potential federal matching funds rather than to continue to fund California's fractured safety net programs.

An estimated 3 million uninsured California adults are under 250% of the FPL. Some of those with children would be covered under the waiver request submitted by the Davis administration. The LAO estimated it would cost \$4.5 billion to cover this whole group. This amount would vary depending on how much of the \$1,500 per person annual cost is offset by the premiums paid by the enrollee placed in the Healthy Families program. Depending on the level of federal matching funds obtained under the waivers, the state's annual share could be reduced to an estimated \$1.2 - 1.8 billion, assuming the state continues to fund the safety net at existing levels.

Throughout the process the author has argued that these new costs could be offset by reduced participation in the numerous safety net programs that currently provide care for these individuals who would presumably be receiving care under the newly expanded Cal Health program. The current state and county effort in this area is roughly \$6.5 billion. Adding childless adults under 250% of the FPL will significantly exacerbate this problem. Our goal should be to increase private coverage, not supplant it with government sponsored coverage.

Bonds

The Legislature will consider various bond proposals before the end of session. The deadline to get a bond on the March ballot is September 15th. Bonds for later next year can be acted on in January.

◆ Cost of Bonds vs. Pay as You Go

Bond financing is considerably more expensive than pay-as-you-go financing. When bonds are sold, the State must pay transaction fees to the bond underwriters, which can run into the millions of dollars in addition to annual interest charges. These costs run into the hundreds of millions or dollars over time and do not provide any additional infrastructure development. For example, for every \$1 billion on G.O. debt issued, the state will have to pay approximately \$1.6 billion (for 20-year bond) or \$1.9 billion (for 30-year bond) in debt service to retire the bonds. This assumes a 20-year bond at 6% annual interest. Therefore, bond financing can be twice as expensive as a straight pay-as-you-go approach.

Bond proposals are under consideration in the following areas.

◆ Energy

Last spring the Legislature authorized \$13.45 billion in bonds for the purchase of energy, but the Treasurer is expected to issue only \$12.5 bonds. Several issues remain before the Treasurer can issue the bonds. On September 6, the CPUC is expected to meet to make decisions on all matters required for the bonds. According to the Treasurer's Office, the remaining issues include: Servicing Agreements/Order; SDG&E Rate Adjustment; Suspension of Retail Choice; Rate Order; and Rate Agreement. In late September, the Treasurer will release its final report and bond covenant documents. The bond sale may not be until November.

◆ Hospitals

California hospitals must comply with seismic retrofit standards by 2030 and they are finding it difficult to comply with this 1994 mandate. AB 1156 (Aroner), which addresses this issue, is currently pending.

◆ Juvenile and Adult Correctional Facilities

Many of California's juvenile halls are dangerously overcrowded and desperately in need of repair and renovation. It is a place where five youths are sometimes stuffed into a cell built for one - and three per cell is common. Over one-third of California's counties are under federal or local court orders to release inmates if their respective jails reach a population cap established by court order. This has resulted in tens of thousands of inmates being released early over the past several years.

Bills currently pending in the Legislature to address this issue include SB 39 (Poochigian) for \$400 million for adult facilities and SB 574 (Polanco) in an unspecified amount for juvenile facilities.

◆ **Voting Equipment**

The November election and the Florida situation have increased calls for updating voting equipment. The majority of California voters (11.4 million of California's 15.7 million registered voters) cast ballots on punch-card systems, which have been in use for decades. Votomatic systems, which use pre-scored punch cards, are those most susceptible to chad being left on the ballot after the voter has finished voting. Approximately 6.5 million Californians vote using this system.

Assemblyman Hertzberg's AB 56, if approved by the Legislature and the voters, would provide funds for counties to purchase updated voting systems (except for those that use pre-scored punch cards). The most obvious choice is touch-screen voting. Several counties have demonstrated the equipment in early voting. Riverside County has completely converted its entire election system to touch screen voting.

Other Issues

Several other issues also may be the subject of late session negotiations and last minute deals. Some of those are highlighted below.

◆ **Workers Compensation**

California's workers' compensation system is currently in a state of turmoil. Many argue that benefits are much too low, yet insurer insolvency continues to grow. Dramatic workers' compensation reform passed by the Legislature in 1993 addressed many of the flaws in the workers' comp system, yet also created some new problems.

As part of the 1993 reforms, the Legislature approved repealing the minimum rate effective January 1, 1995, which allowed premium rates to float as the market dictated. The open competition between insurers for workers' compensation business resulted in premium reductions that have been, at times, lower than the actual cost of providing the insurance. Due in large part to these poor business practices, many insurers have become insolvent and employers are beginning to see drastic premium hikes. Premium increases in 2000 ranged from 5% to 24%. This increase in insurance premiums for workers' compensation insurance hit small business employers especially hard.

Despite the industry instability, many believe that an increase in benefits is now necessary. For the past two years, Legislative Democrats have sent a bill to the Governor that would have increased workers' compensation benefits anywhere from 15% to 25%, over six years. Governor Davis ultimately vetoed both measures when negotiations over the amount of increase in benefits stalled.

Senator Burton's SB 71, currently a spot bill, is likely this year's benefit increase bill. The Governor has indicated support of a benefit increase this year; however, it is still unclear how much of an increase California's businesses and economy can handle.

◆ **California Earthquake Authority**

Currently, three measures are working their way through the legislature related to the operations of the CEA, which are likely to end up in conference committee. A recently released report detailed ways in which the CEA could improve operations.

A conference report should improve the survivability of the CEA after a major earthquake, while expanding investment opportunities that would lower the cost of reinsurance for the CEA. Some Democrat members have expressed interest in reorganizing the "layers" of insurance coverage that underwrites the CEA to require a greater contribution from insurers in the event of a quake. Currently the CEA has various layers of insurance, reinsurance and cash on hand that would be needed in the event of a quake. If the quake is large enough all layers of coverage could be exhausted. Any attempt to reorganize the contractual responsibilities of the CEA represents a major change in policy and should be resisted.

◆ **Fully Protected Species**

California has a provision in law that fully protects a selected list of about 37 species that are extremely rare or endangered (even though some on the list are not even listed under the state or federal endangered species laws). The Department of Fish and Game has decided that, under the fully protected species provisions, they are not authorized to issue incidental take permits. The list includes species such as the bighorn sheep, the American peregrin falcon, the trumpeter swan, the California condor, and the sandhill crane to name a few. This has caused considerable problems and in fact threatens further progress for some significant proposed development projects such as the San Francisco Airport/BART expansion, CALFED projects, the Colorado River 4.4 Plan and the Seitz Reservoir.

Two pending bills deal with the issue of fully protected species: AB 1561 (Kelley) and AB 985 (Florez). While negotiations are ongoing, environmentalists are withholding their support of any reform to the fully protected species law that would allow incidental take unless they get reforms they seek to the California Endangered Species Act (CESA) and the Natural Community Conservation Planning Program (NCCP). The reforms they want could be quite harmful to the programs and would further delay or halt development. Both bills are currently "spot" bills that would contain any compromise language.

◆ **Predatory Lending**

Predatory lending has been identified as a pandemic societal problem where the elderly and minorities are duped into receiving loans they can not repay, often times resulting in the loss of their homes. A loan is considered predatory when a homeowner (or buyer) enters into a loan agreement and does not have the financial wherewithal to repay the loan. The legislative

solutions proposed this session have been abundant. One bill, however – AB 489 (Migden) – is the likely omnibus bill to reform the lending industry in California. Industry has unanimously objected to the proposed changes which include severe criminal and civil penalties. Such penalties include jail time and personal, as well as corporate, fines for industry CEOs and employees. The likely result of such legislation will be a mass exodus of lending institutions from California, and the general unavailability of home loans for Californians, especially the elderly and those of modest means.

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